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July 8, 2004

Ms. Jennifer Johnson, Secretary  
Board of Governors of the Federal Reserve System  
20<sup>th</sup> Street and Constitution Avenue, N.W.  
Washington, DC 20551  
[regs.comments@federalreserve.gov](mailto:regs.comments@federalreserve.gov)

**SUBJECT: Risk-Based Capital Standards: Trust Preferred Securities and the Definition of Capital, Docket No. R-1193**

Dear Ms. Johnson:

The Massachusetts Bankers Association ("MBA") has reviewed proposed changes referenced above, and reviewed its findings with its members. The Cooperative Bank concurs with the MBA's position and we appreciate the opportunity to comment on the Federal Reserve System Board ("Board") proposal to allow the continued inclusion of outstanding and prospective issuances of trust preferred securities in Tier 1 capital for bank holding companies, subject to new limitations.

**Background and Proposal**

In 1996, the Board approved the inclusion of bank holding companies (BHC's) Tier 1 capital of minority interest in the form of trust preferred securities based on factors such as their qualification under generally accepted accounting principals (GAAP), ability to absorb losses more broadly in the consolidated banking organization and competitive equity factors. Trust preferred securities are favored because of their ease of use and cost efficiency.

Under the proposal, the Board would allow BHC's to continue applying existing rules which permit up to 25% of trust preferred securities and cumulative perpetual preferred stock in Tier 1 capital. After March 31, 2007, BHC's would have to deduct goodwill from their Tier 1 capital before calculating the 25% limit. The amount of trust preferred securities and certain other elements in excess of the limit could be included in Tier 2 capital, up to 50% of a banking organization's Tier 1 capital. Internationally-active BHCs would generally be expected to limit trust preferred securities and certain other capital elements to 15% of Tier 1 capital elements, net of goodwill.

## **Comment**

We commend the Board for its efforts to strengthen the definition of regulatory capital for bank holding companies while acknowledging that trust preferred securities are an important instrument for financial institutions. MBA members, consisting in the majority of small to medium sized community banks, and a few large regional banks, utilize trust preferred securities as an important way to free up and / or lower the after-tax cost of capital. We commend the Board for continuing to permit the inclusion of trust preferred securities in Tier 1 capital.

We wish to comment on the proposed three-year transition period for BHC's to meet the new stricter requirements. A five year transition would provide BHC's more time to accommodate longer-term binding contracts dating back to as early as 1996 when the Board initially permitted the use of trust preferred securities in Tier 1 capital. In addition, we would also comment that the Board does not need to formalize the standard that banks limit their inclusion of innovative products such as trust preferred securities to 15% of Tier 1 capital. As the Board has acknowledged in its proposal, internationally-active large banking organizations are subject to more rigorous market discipline, and do not exhibit excess reliance on trust preferred securities or other similar instruments.

While this ruling is important for all member banks, it is particularly meaningful to Massachusetts banks in mutual governance form which would otherwise rely on retained earnings as the sole means of increasing capital. By utilizing trust preferred securities, mutual banks can pursue growth strategies which require extra capital, without changing their mutual status. This is a critical benefit for local communities, and the banks that serve them.

We encourage the Board to work with other banking regulators to foster continued acceptance of the treatment of trust preferred securities in Tier 1 capital.

Thank you for the opportunity to submit comments regarding the proposal.

Sincerely,

Paul M. Ladouceur  
President & CEO